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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 170

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

TWIN BELL OIL SYNDICATE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 14–27) is reported in 26 B. T. A. 172. The opinion of the Circuit Court of Appeals (R. 194–214) is reported in 70 F. (2d) 402.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered April 12, 1934 (R. 215). The petition for a writ of certiorari was filed July 12, 1934, and

was granted October 8, 1934. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether an assignee of an oil lease is entitled to the full depletion allowance of 27½ percent of gross income from the leased wells or whether such allowance must be equitably apportioned among the lessor, lessee, and assignee.

STATUTES AND REGULATIONS INVOLVED

The pertinent statutes and regulations involved are set forth in the Appendix, *infra,* pp. 22–25.

STATEMENT

The facts as found by the Board of Tax Appeals R. 15–20) and as stipulated in part (R. 84–168) by the parties are as follows:

The taxpayer is a California syndicate organized in 1922 for the purpose of acquiring a certain oil and gas lease and operating it (R. 36–41). Both the Board and the court below have held that the syndicate is to be treated as a corporation for Federal income-tax purposes.

The original lessee of the properties was one F. A. Andrews, who secured a twenty-year lease from the owner, W. O. Batson, in December 1921. In addition to certain monthly rentals to be paid until drilling should commence the lessee agreed to

pay as rental or royalty for the land "one-sixth (⅙) of all oil produced and saved therefrom, said payment to be made in money or in kind at the Lessor's option" (R. 86–90).

On February 10, 1922, Andrews assigned all of his right, title, and interest in the lease to Thomas H. Lipps, who agreed to perform all of the covenants of Andrews and that in addition to the one-sixth royalty agreed to be paid to the lessors he would pay to Andrews "one-twelfth ($^{1}/_{12}$) of all petroleum, oil, gas, and other oil products, and casing-head gasoline, produced and saved from each and all wells" on the property either in cash or in kind (R. 95–97).

On April 25, 1922, Lipps assigned all his right, title, and interest in the lease to the trustees of the syndicate, who agreed to comply with all of the terms and conditions of the original lease and also of the assignment by Andrews (R. 103–105).

The one-sixth royalty and the one-twelfth royalty paid to Andrews during the taxable years 1925, 1926, and 1927 were as follows (R. 18):

Year	Batson Royalties	Andrews Royalties
1925	$159,853.20	$79,926.60
1926	143,253.02	71,626.51
1927	70,946.34	35,473.17

In the audit of the taxpayer's returns for 1925, 1926, and 1927, the Commissioner held that the above-mentioned royalties should be deducted from

the gross income from the wells before computing the 27½-percent deduction for depletion allowed under Section 204 (c) (2) (R. 18–19). The Commissioner determined deficiencies as the result of this and other adjustments, and the taxpayer appealed to the Board.

The Board sustained the Commissioner's allowance for depletion, but decided against the Commissioner on another issue. Both parties appealed. The Circuit Court of Appeals for the Ninth Circuit reversed the Board on the issue concerning depletion, which was one of two issues in the syndicate's appeal. That court held that the 27½-percent deduction should be computed on the gross income of the syndicate without deduction for the rents and royalties. The other issues involved in the case were decided for the Government and are not here involved.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the term "gross income from the property" as used in Section 204 (c) (2) of the Revenue Act of 1926, *infra,* means gross income of the taxpayer as defined in Section 213 (a) of that Act, *infra.*

2. In holding that Section 204 (c) (2) should be construed independently of Section 234 (a) (8).

3. In holding that in the case of an assignee paying rents and royalties to its assignor and

the lessor the term "gross income from the property" in Section 204 (c) (2) means gross income including such rents and royalties.

4. In failing to hold that the "gross income from the property" on which the percentage deduction for depletion is based under Section 204 (c) (2) means gross income less rents and royalties.

SUMMARY OF ARGUMENT

Section 234 (a) (8) of the Revenue Act of 1926, which provides for depletion deduction, and Section 204 (c) (2), which prescribes the rate or measure of the allowance, are to be read *in pari materia,* and Section 204 (c) (2) must be construed in the light of the mandate of Section 234 (a) (8) that depletion must be equitably apportioned between lessor and lessee. The only way to give effect to the apportionment provision is to allow the lessor 27½ percent on his share of the total production from the well, and the lessee 27½ percent on his share.

Under the construction adopted by the court below the various parties having an interest in the properties together are allowed deductions equal to 27½ percent of five-fourths of the gross income of the properties or a greater allowance for depletion than the owner himself would be entitled to if he operated the property. Moreover, the court's construction permits the taxpayer to measure his depletion allowance on another's income, and has

the effect of allowing the taxpayer a double deduction. Congress clearly did not intend such results.

The legislative history of Section 204 (c) (2) does not disclose any intention on the part of Congress to do away with the requirement of apportionment between lessor and lessee in the case of percentage deduction. Further, the clarifying provisions in the 1934 Act make it clear that Congress never intended that a lessee's depletion allowance should be based on rents or royalties paid by him in respect to the property.

ARGUMENT

In the present case the taxpayer was a sublessee of certain oil properties. It received the total income from the sale of the oil and gas produced but was obligated to pay the lessor one-sixth and its assignor one-twelfth, a total of one-fourth of the production. In computing the taxpayer's taxable net income the Commissioner allowed as a depletion deduction 27½ percent of the taxpayer's share of the oil produced; that is, 27½ percent of three-fourths of the production. The court below, however, allowed 27½ percent of the entire production, despite the fact that the taxpayer was entitled under Section 234 (a) (1) of the Revenue Act of 1926 (*infra*, p. 23) to deduct from its gross income the royalty payments, and also despite the fact that those to whom the taxpayer made royalty payments were likewise entitled to a 27½ percent depletion allowance on the royalties paid to them. In this we submit the court clearly erred.

It is fundamental, of course, that deductions from gross income are purely matters of legislative grace, and a taxpayer is entitled to no deduction unless the statute plainly authorizes it. The deduction for depletion in the case of corporations [1] is set forth in Section 234 (a) (8) of the Revenue Act of 1926 (*infra,* p. 24) which provides that a deduction shall be allowed:

> In the case of mines, oil and gas wells * * * for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. *In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee.*[2] (Italics supplied.)

Section 204 (c) (*infra,* p. 22) provides that the basis upon which depletion is to be allowed is the same as that provided in the case of a sale, with certain exceptions. One of these exceptions is set forth under subdivision (2), upon which the court relied entirely for its conclusion, as follows:

> In the case of oil and gas wells the allowance for depletion shall be 27½ per centum of the gross income from the property dur-

[1] The taxpayer is an association taxable as a corporation.

[2] Section 214 (a) (9) (*infra,* p. 23) grants an allowance under similar conditions to individuals.

> ing the taxable year. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph.

It is apparent that the authority for the depletion deduction is contained only in Section 234 (a) (8). Section 204 (c) (2) merely provides the rate or measure of the allowance in those cases falling within Section 234 (a) (8). Section 204 (c) (2) is dependent for its operation upon Section 234 (a) (8). It is necessary, therefore, to read the two sections together so as to give a reasonable effect to both provisions. *Ginsberg & Sons* v. *Popkin*, 285 U. S. 204, 208; *Helvering* v. *New York Trust Co.*, 292 U. S. 455. And Section 204 (c) (2) must be construed in the light of the mandate of Section 234 (a) (8) that depletion must be equitably apportioned between lessor and lessee. So construed, it seems reasonably clear that Congress intended that the reasonable allowance for depletion in the case of oil and gas wells on leased property should be 27½ percent of the gross income "from the property", and that this allowance should be equitably apportioned between the lessor and lessee. The taxpayer, as lessee, had a three-fourths interest in the oil produced from the well, the other one-fourth interest being in Batson, the lessor, and Andrews, the original lessee. The depletion allow-

ance with respect to the oil and gas wells should be 27½ percent of the gross income from the wells equitably apportioned between the taxpayer, Batson, and Andrews.

The court below reached its conclusion by considering Section 204 (c) alone and construed the words "gross income from the property" as used in that subsection as meaning the taxpayer's gross income as defined in Section 213 of the Act (*infra*, p. 22). But in this the court plainly erred. Clearly the words "gross income from the property", as employed in Section 204 (c) (2), did not include income from other businesses separate and distinct from the operations of the oil properties themselves. In *United States* v. *Dakota-Montana Oil Co.*, 288 U. S. 459, 461, this Court referred to the percentage depletion provision as follows:

> But the "discovery value" provision was eliminated from the act of 1926, which is applicable here, and the taxpayer was permitted to calculate depletion on the basis of cost alone, Sec. 204 (c), or else to deduct an arbitrary allowance, fixed by the statute, without reference to cost or discovery value, at 27½ percent of *gross income from the well.* [Italics supplied.]

In *Darby-Lynde Co.* v. *Alexander*, 51 F. (2d) 56 (C. C. A. 10th), certiorari denied, 284 U. S. 666, the taxpayer argued that the proceeds from the sale of the oil property itself (in addition to the proceeds from the sale of oil and gas) constituted gross income and should be included in the gross income on

which the percentage depletion deduction was based. But the court rejected that argument, holding that the term "gross income from the property" as employed in Section 204 (c) (2) meant gross income from production. See also *Macon Oil & Gas Co.* v. *Commissioner,* 23 B. T. A. 54; *Fritz* v. *Commissioner,* 28 B. T. A. 408. Compare also *Houston Production Co.* v. *United States,* 4 F. Supp. 715 (S. D. Tex.); G. C. M. 2315, VI–2 Cumulative Bulletin 21. It is clear, therefore, that "gross income from the property" refers to something other than the taxpayer's statutory gross income.

It is to be observed in this connection that Section 204 (c) (2) provides first for a depletion allowance of "27½ per centum of the gross income from the property", and second that "such allowance shall not exceed 50 per centum of the net income *of the taxpayer* (computed without allowance for depletion) from the property." (Italics supplied.) We think the choice of language here is significant. The allowance in the first clause of the paragraph is based on the "gross income from the property", while the limitation in the second clause is fixed at 50 percent of "the net income *of the taxpayer* * * * from the property." The omission of the phrase "of the taxpayer" in the first clause and the insertion of those words in the second is susceptible of the interpretation that in the first Congress was dealing with gross income produced by the property irrespective of whether technically it was the taxpayer's gross income, or that of his

lessor, or both combined, while in the second, Congress was dealing with the net income of the particular taxpayer. In other words, Congress intended to allow for depletion a flat 27½ percent of the total income produced by the well, irrespective of to whom this income was attributable; that in the case of leases this total allowance is to be apportioned equitably between the lessor and lessee, but in no event is the allowance to be greater than 50 percent of the taxpayer's net income. This is the construction placed upon the phrase "gross income from the property" by the Board of Tax Appeals in the instant case (R. 24–25), and in *Greensboro Gas Co.* v. *Commissioner,* 30 B.T.A. 1361.

But whether those words are to be construed as meaning gross production from the property, as held by the Board, or the taxpayer's gross income from the property, they must still be read in the light of the equitable apportionment provision in Section 234 (a) (8). The Commissioner solved the problem of apportionment in the present case by holding that the phrase "gross income from the property" meant the gross income from production less the amounts which the taxpayer was obliged to pay to his assignor and to the lessor, that is, three-fourths of the total. In that way the taxpayer was allowed 27½ percent of the gross income from production, which it was permitted to retain, and his assignor and the lessor together would receive an allowance based upon 27½ percent of the

remaining one-fourth.[3] This was clearly a reasonable construction of the two sections when read together. See *Night Hawk Leasing Co.* v. *Burnet,* 57 F. (2d) 612 (App. D. C.).

It is a cardinal rule of statutory construction that when the language of a statute is of doubtful meaning, or when adherence to the strict letter would lead to injustice or absurdity, or result in contradictory provisions, it devolves upon the court to ascertain the true meaning. If possible, the statute will be construed so as to avoid inequity and to achieve a reasonable result. *United States* v. *Katz,* 271 U. S. 354, 357; *In re Chapman,* 166 U. S. 661; *United States* v. *Kirby,* 7 Wall. 482, 486–487. The construction placed on Section 204 (c) (2) by the court below violates these principles.

Obviously the lessor and the taxpayer's assignor have an economic interest in the property and are entitled to a deduction for depletion based on 27½ percent of the one-fourth royalty that they together received. *Palmer* v. *Bender,* 287 U. S. 551; *Helvering* v. *Falk,* 291 U. S. 183; *Green* v. *Commissioner,* 26 B. T. A. 1017. But under the construction of the statute by the court below the taxpayer, the lessor, and the assignor together would be allowed a deduction equal to 27½ percent of five-fourths of

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[3] As pointed out by the Board (R. 25), the allowance determined by the Commissioner is exactly the same as would have been determined had the Commissioner taken 27½ percent of the total gross income from the property and apportioned three-fourths of the amount to the taxpayer.

the gross income from the property. It is unreasonable to suppose that Congress intended that a multiplication of interests in the property should result in a greater allowance for depletion than the owner himself would be allowed if he operated the property.[4] It is far more reasonable to assume that Congress intended that the percentage deduction allowable to all having an economic interest should amount in the aggregate to 27½ percent of the gross income from the property, that is, from production, and that this amount should be equitably apportioned between all having such interest. There is no apportionment under any other theory.

Moreover, it is unreasonable to suppose that Congress intended that a taxpayer should measure his depletion allowance by another's interest in the property. Yet the decision below has that result. The fundamental purpose of the depletion statutes has always been to return to a taxpayer, whatever

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[4] The discussions before the Senate Finance Committee, where the amendment which ultimately became Section 204 (c) (2) originated, indicate that the framers of this legislation had in mind the abolition of discovery depletion and the substitution of a flat percentage based on gross production from the operation of the properties. See Hearings before the Committee on Finance on H. R. 1, 69th Cong., 1st Sess., pp. 147, *et seq.*, particularly at pp. 152–158, 178–179, 180. The discussions dealt only with the case of an operating owner, but in basing the percentage allowance on gross production, the Committee clearly did not intend in the case of leases that the total allowance to lessor and lessee should exceed the 27½ percent allowed to the operating owner.

his interest may be, a reasonable allowance for the exhaustion *of his interest* in the property caused by the depletion of the natural resource during the taxable year. *Lynch* v. *Alworth-Stephens Co.*, 267 U. S. 364; *Palmer* v. *Bender, supra; Night Hawk Leasing Co.* v. *Burnet, supra.* The insertion of the percentage depletion provision in the 1926 Act wrought no change in this fundamental purpose. The provision was inserted merely to put an end to the difficulties occasioned by the computation of depletion on the basis of discovery value in the case of oil and gas wells. S. Rep. No. 52, 69th Cong., 1st Sess., pp. 17–18; H. Rep. No. 356, 69th Cong., 1st Sess., pp. 31–32. Congress, in the 1926 Act, did not intend to break with the past and narrow the functions of the depletion allowance. The real nature and purpose of the depletion provisions remained unchanged. *United States* v. *Dakota-Montana Oil Co., supra.* In permitting the taxpayer here to take depletion based on royalties paid over to the lessor and its assignor the court below has allowed the taxpayer depletion based on another's interest in the depletable asset and without regard to the taxpayer's interest in the property, thus violating the fundamental purpose of the depletion statutes. We submit Congress never intended that the percentage depletion provisions should have that effect.

It may be true that the portion of the income from the property which the taxpayer pays over in the form of royalties to its assignor and the original

lessor is required to be reported in its gross income in its return (*Comar Oil Co.* v. *Burnet,* 64 F. (2d) 965 (C. C. A. 8th), certiorari denied, 290 U. S. 652), but these royalties did not represent an exhaustion of the taxpayer's interest in the oil reserve for which it should have a depletion allowance. In many cases the pipe-line company or other purchaser of the oil production recognizes the different economic interests in the oil properties and as a matter of practice instead of paying the operating lessee the full price paid for the entire production, pursuant to a division order, make payments directly to the various interested parties in accordance with their several economic interests; so that in those cases a taxpayer like the one here would receive payment for only three-fourths of the oil produced and the assignor and the lessor together would receive directly from the purchaser payment for the remaining one-fourth. The practice in those cases is for the operating lessee to report in his gross income only the payments actually received by him, and for the others in interest to report the amounts received by them. This practice has been recognized and approved by the Treasury Department. Thus the question presented in this case can not arise in many cases because the taxpayer's "gross income from production" usually includes only the fraction of production which, under the lease, the lessee is permitted to retain, excluding royalties paid directly to the lessor or others in interest. It

so happened that in this case the lessee received payment for the entire production and was required to make disbursements to its assignor and to the lessor. In other words, it acted as a collecting agent for the lessor and its assignor, a conduit through which the royalty payments passed. And, unlike the *Comar* case, the taxpayer here was permitted to deduct under Section 234 (a)(1) of the Act, *infra*, p. 23, the current royalties paid over by it in the form of rent.[5] The effect is the same as if it had included in its gross income only three-fourths of the total production from the wells, as is the practice in the cases above referred to. We submit that Congress never intended that a taxpayer in a situation like this, who receives royalties for the benefit of another, who is obligated to pay such royalties immediately over to those entitled thereto, and who

[5] While the record does not affirmatively show that this taxpayer deducted royalties paid by it under Section 234 (a) (1), in its petition to the Board it asserted that it was entitled to such deductions (R. 6) and we are advised by the Treasury that as a matter of fact such deductions were claimed on the several tax returns and were allowed by the Commissioner. This case differs from the *Comar* case in that here the royalties were payable currently from production over the life of the lease and were considered by both the taxpayer and the Commissioner as in the nature of current rental payments; whereas in the *Comar* case the royalties involved were payable out of the first runs of oil and gas, and since the benefits of such payments extended beyond the current year, they were more in the nature of capital expenditures and not deductible under Section 234 (a) (1).

deducts such payments from its gross income, should have a greater depletion allowance than the lessee in the case where payments are made directly by the pipe-line company or other purchaser. To permit the taxpayer here to deduct royalty payments in determining its taxable income, and at the same time to include such royalties for the purpose of determining its depletion allowance, is in effect to allow a double deduction, a result clearly not intended by Congress.

Our interpretation of the statute results in no undue hardship to the taxpayer. Section 204 (c) (2) provides that in no case shall the percentage allowance be less than it would be if computed without reference to that paragraph. Under this provision the taxpayer is always permitted to have his depletion computed on the basis of cost if the computation under that method results in a greater deduction. Thus the taxpayer is always assured of having a return of his capital, and our construction of the statute works no hardship on him, whereas the court's construction achieves an unreasonable result.

That our construction is the proper one is demonstrated, we submit, when we consider the legislative history of the provisions involved. The legislative history of Section 204 (c) (2) does not disclose any intention on the part of Congress to do away with the requirements of apportionment between the

lessor and lessee in the case of the percentage deduction. As stated above, the provision was inserted merely to put an end to the difficulties occasioned by the computation of depletion based on discovery value. S. Rep. No. 52, 69th Cong., 1st Sess., pp. 17–18; H. Rep. No. 356, 69th Cong., 1st Sess., pp. 31–32. Thus we must continue to apply the equitable apportionment requirements and construe that provision in conjunction with Section 204 (c) (2). See also footnote 4, p. 13, *supra.*

Section 204 (c) (2) of the 1926 Act was reenacted in identically the same language as Section 114 (b) (3) of the Revenue Act of 1928. The Commissioner construed both of these sections as requiring the exclusion from the gross income of rents and royalties in computing the 27½ percent deduction for depletion under both the 1926 and 1928 Acts. See *Greensboro Gas Co.* v. *Commissioner, supra.* Thereafter, the same provisions were reenacted as Section 114 (b) (3) of the Revenue Act of 1932, p. 24, *infra,* with an amendment which added the words "excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property." Thus Congress incorporated in the 1932 Act the prior practice of the Commissioner and that Act is entirely in accord with the position taken by us here. The legislative history of the 1932 amendment indicates that the purpose of the amendment

was to clarify the existing law, not to change it. The amendment in question originated in the Senate and was offered under the following circumstances (Cong. Record, Vol. 75, Part 10, pp. 11629, 11630):

> Mr. SMOOT. * * * I may also say that I have 10 or 11 other amendments of a *clarifying* nature which I want to offer following the one now offered.
>
> * * * * *
>
> Mr. KING. I think my colleague should state that the amendments which he is about to offer were all presented to the committee, considered by the committee, and unanimously agreed to by it.
>
> * * * * *
>
> Mr. SMOOT. Yes; and they were all prepared by the Treasury Department.

The amendment to Section 114 (b) (3), No. 53, was one of the clarifying amendments so offered by Mr. Smoot and was adopted by the Senate. In conference the amendment was accepted by the House and in its conference report it was stated (H. Conference Rep. No. 1492, 72d Cong., 1st Sess., p. 14):

> This amendment *makes it clear* that in computing the gross income from the property, for the purpose of determining the allowance for percentage depletion in the case of oil and gas wells, there shall be excluded from such gross income an amount

> equal to any rents or royalties paid or incurred by the taxpayer in respect of the property * * *. [Italics supplied.]

We submit that this amendment is declaratory of existing law, and was intended to clarify rather than to alter the provisions of the previous Act. Congress was merely enacting into law the correct interpretation of the existing law. See *Luckenbach S. S. Co.* v. *United States,* 280 U. S. 173, 182–183; *Commissioner* v. *Liberty Nat. Co.,* 58 F. (2d) 57 (C. C. A. 10th); *Helvering* v. *New York Trust Co., supra.*

We submit that the court below reached a result opposed to the clear intent of Congress by construing Section 204 (c) (2) independently of Section 234 (a) (8), when the two can only be intelligently construed together. It thus violated the fundamental principle of statutory construction above adverted to—that a statute is to be construed as a whole so as to give a reasonable effect to all its provisions. The construction for which we contend is not inconsistent with the express language employed in Section 204 (c) (2). But even if the literal language would compel the interpretation made by the court below, it should not be followed when to do so makes it impossible to give effect to the probable intent of Congress as expressed in the statute as a whole. *Helvering* v. *New York Trust Co., supra; Rockford Life Insurance Co.* v. *Helvering,* 292 U. S. 382.

CONCLUSION

The decision of the Circuit Court of Appeals should be reversed.

Respectfully submitted.

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OCTOBER 1934.

APPENDIX

REVENUE ACT OF 1926, C. 27, 44 STAT. 9

SEC. 204. (c) The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the same as is provided in subdivision (a) or (b) for the purpose of determining the gain or loss upon the sale or other disposition of such property, except that—

* * * * *

(2) In the case of oil and gas wells the allowance for depletion shall be 27½ per centum of the gross income from the property during the taxable year. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph. [U. S. C. App., Title 26, Sec. 935.]

SEC. 213. For the purposes of this title, except as otherwise provided in section 233—

(a) The term "gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership

or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period. [U. S. C. App., Title 26, Sec. 954.]

* * * * *

SEC. 214. (a) In computing net income there shall be allowed as deductions:

* * * * *

(9) In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. In the case of leases the deduction allowed by this paragraph shall be equitably apportioned between the lessor and lessee; [U. S. C. App., Title 26, Sec. 955.]

* * * * *

SEC. 234. (a) In computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

(1) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered, and including

rentals or other payments required to be made as a condition to the continued use or possession of property to which the corporation has not taken or is not taking title, or in which it has no equity;

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(8) In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee [U. S. C. App., Title 26, Sec. 986].

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SEC. 114. * * *

(b) Basis for Depletion—

(3) Percentage depletion for oil and gas wells.—In the case of oil and gas wells the allowance for depletion shall be 27½ per centum of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph (U. S. C. Sup. VII, Title 26, Sec. 114.)

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ART. 221. *Depletion in the case of oil and gas wells.*—Under section 204 (c) (2), in the case of oil and gas wells, a taxpayer may deduct for depletion an amount equal to 27½ percent of the gross income from the property during the taxable year, but such deduction shall not exceed 50 percent of the net income of the taxpayer (computed without allowance for depletion) from the property. In no case shall the deduction computed under this paragraph be less than it would be if computed upon the basis of the cost of the property or its value at the basic date, as the case may be. In general, "the property", as the term is used in section 204 (c) (2) and this article, refers to the separate tracts or leases of the taxpayer.

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